DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER 05-0299
SALES AND USE TAX
For Tax Period 2001-2002

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Issues

I. Sales and Use Tax –Rentals of Spaces for Beauty Shops

Authority: IC § 6-8.1-5-1(b); 6-2.5-4-4(a).

The Taxpayer protests the imposition of use tax on rentals of spaces for beauty shops.

II. Sales and Use Tax – Bariatric Beds and Equipment

Authority: IC § 6-2.5-5-18(b); 45 IAC 2.2-5-27(b).

The Taxpayer protests the imposition of use tax on bariatric beds and equipment.

III. Sales and Use Tax –Water Heaters

Authority: IC § 6-2.5-3-2; Sales Tax Information Bulletins #60 dated November 2000 and December 2001.

The Taxpayer protests the imposition of use tax on water heaters.

IV. Tax Administration-Imposition of Negligence Penalty

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2(b); 45 IAC 15-11-2(c).

The taxpayer protests the imposition of the negligence penalty.

Statement of Facts

The taxpayer is a limited partnership that operates nursing homes. Pursuant to an audit, the Indiana Department of Revenue, hereinafter referred to as the "Department," assessed additional use tax, interest, and penalty for the tax period 2001-2002. The Taxpayer also requested refunds of certain sales taxes that it had paid. The Department denied a portion of the requests for refund. The taxpayer protested a portion of the assessments and certain of the refund denials. A hearing was held and this Letter of Findings results.

I. Sales and Use Tax –Imposition on Rentals of Spaces for Beauty Shops

Discussion

Beauticians rented space in the Taxpayer's nursing homes. The Department imposed sales tax on the Taxpayer's receipts from the furnishing of these spaces for beauty salons. The Taxpayer protested this imposition of sales tax.

Indiana Department of Revenue assessments are prima facie evidence that the tax assessment is correct. IC § 6-8.1-5-1(b). The taxpayer bears the burden of proving that the assessment is incorrect. Id.

Sales tax was imposed on the taxpayer's receipts from accommodations pursuant to the following provisions of IC § 6-2.5-4-4(a):

> A person is a retail merchant making a retail transaction when the person rents or furnishes rooms, lodgings, or other accommodations, such as booths, display spaces, banquet facilities, and cubicles or spaces used for adult relaxation, massage, modeling, dancing, or other entertainment to another person:
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> (1) if those rooms, lodgings, or accommodations are rented or furnished for periods of less than thirty (30) days: and
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> (2) if the rooms, lodgings, and accommodations are located in a hotel, motel, inn, tourist camp, tourist cabin, gymnasium, hall, coliseum, or other place, where rooms, lodgings, or accommodations are regularly furnished for consideration.

The Taxpayer first argued that it did not rent accommodations to the beauticians. Rather, the Taxpayer suggested that it was in a profit-sharing arrangement with the beauticians and merely supplied the space as part of the profit-sharing arrangement.

"Rent" is defined in Black's Law Dictionary 1297 (6th ed.1990) as follows:

> Consideration paid for use or occupation of property. In a broader sense, it is the compensation or fee paid, usually periodically, for the use of any rental property, land, buildings, equipment, etc.

In this situation, the Taxpayer allowed beauticians to use space for their business in exchange for the consideration of a share of the beauticians' profits. The arrangements were memorialized in formal Agreements signed by both the beauticians and a representative of the Taxpayer. In some of the nursing homes, the income received from allowing the beauty salons to use space in the Taxpayer's nursing homes were listed in the accounting books as "rent." Clearly, the Taxpayer actually rents space for the beauty shops.

The issue to be determined is whether or not the rents are subject to the sales tax pursuant to IC § 6-2.5-4-4(a).

The law requires that sales tax shall be collected if a retail merchant furnishes space in return for consideration for less than thirty (30) days. In this situation, the Taxpayer was a retail merchant renting space to the beauticians. The Taxpayer provided copies of the agreements executed between the Beauticians and Taxpayer. These agreements established that the spaces were rented to the beauticians for longer terms than thirty day periods. Since the accommodations were provided for periods of more than thirty days, the Taxpayer is not required to collect and remit sales tax on the rentals of the spaces for beauty salons.

Finding

The Taxpayer's protest is sustained.

II. Sales and Use Tax –Imposition on Bariatric Beds and Equipment

Discussion

The Taxpayer paid sales tax on the rental of bariatric beds and other bariatric equipment. During the audit process, the Taxpayer requested a refund of the sales taxes paid on these items. The Department denied that request. The Taxpayer protested the denial.

The Taxpayer contended that the bariatric beds and other bariatric equipment qualified for exemption from the sales tax pursuant to IC § 6-2.5-5-18(b) as follows:

> Rentals of durable medical equipment and other medical supplies and devices are exempt from the state gross retail tax, if the rentals are prescribed by a person licensed to issue the prescription.

For the purposes of sales and use tax, the term "prescription" is defined in the Regulations at 45 IAC 2.2-5-27(b) as follows:

> The term "prescribed" shall mean the issuance by a person described in paragraph 1 of this regulation of a certification in writing that the use of the medical equipment supplies and devices is necessary to the purchaser in order to correct or to alleviate a condition brought about by injury to, malfunction or, or removal of a portion of the purchaser's body.

The Taxpayer argued that it qualified for this exemption because physicians wrote prescriptions for particular patients to use the bariatric beds and equipment. Those particular patients suffered from the disease of obesity. According to the definition of "prescribed" for sales and use tax purposes, the bariatric equipment could only be prescribed by a physician if the equipment were used to treat the medical condition of obesity. The bariatric beds and bariatric equipment were larger and sturdier. They stood up under the additional weight and stress of the obese patients. The bariatric beds and other bariatric equipment did not, however, have any therapeutic purpose. They did not aid in the alleviation or correction of the patients' medical condition of obesity. Therefore, they could not be "prescribed" as that term is used for sales and use tax purposes.

Finding

The taxpayer's protest to the refund denials is respectfully denied.

III. Sales and Use Tax –Imposition on Water Heaters

Discussion

The Taxpayer purchased several installed water heaters during the tax period. The Department assessed use tax on these installed water heaters pursuant to IC § 6-2.5-3-2. The Taxpayer protested the imposition contending that the installed water heaters were real property and not subject to the imposition of sale or use tax. The Taxpayer based this assertion on Sales Tax Information Bulletin #60 dated April 2004 which specifically lists water heaters as real property.

The Taxpayer erred in applying the April 2004 Sales Tax Information Bulletin to the water heaters installed during the tax period 2001-2002. The Sales Tax Information Bulletins #60 dated November 2000 and December 2001 were the applicable bulletins during the tax period. Each of these bulletins had the same language concerning water heaters as follows:

> Persons selling and installing personal property such as manufacturing equipment, carpeting, appliances, water softeners, water heaters, garage door openers, telephone or intercom systems under a "lump sum purchase price" are not construction contractors. However, the sales and installation of these properties do result in the conversion of tangible personal property into realty. Therefore, these persons must collect the Indiana sales tax on the purchase price of the personal property and all incidental materials used to install the personal property.
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> The retail merchant must list separately on its invoices any charges for services not specifically taxable and the purchase price for tangible personal property which is taxable. If the service charges are not separately stated as required, the entire invoice amount will be taxable as a unitary transaction.

In the instances where the Department had an itemized listing for the cost of the materials, the Department assessed use tax only on the cost of the materials such as reference #1482 on March 1, 2001. Otherwise, if no separate listing of the cost of the materials was provided, the Department properly imposed use tax on the entire cost of the lump sum water heater installation contract.

Finding

The Taxpayer's protest is respectfully denied.

IV. Tax Administration-Imposition of Negligence Penalty

Discussion

The Taxpayer also protested the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

The standard for waiving the negligence penalty is given at 45 IAC 15-11-2(c) as follows:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full

amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

(1) the nature of the tax involved;
(2) judicial precedents set by Indiana courts;
(3) judicial precedents established in jurisdictions outside Indiana;
(4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
(5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

The Taxpayer provided substantial documentation to indicate that the negligence penalty does not apply in this situation.

Finding

The Taxpayer's protest is sustained.

KMA/BK/DK-December 1, 2006